Agenda Date: 08/16/06
Agenda Item: 2D

STATE OF NEW JERSEY
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102
www.bpu.state.nj.us

ENERGY

IN THE MATTER OF THE PETITION OF PIVOTAL UTILITY HOLDINGS, INC. d/b/a ELIZABETHTOWN GAS COMPANY TO ESTABLISH A PIPELINE REPLACEMENT PROGRAM COST RECOVERY RIDER

ORDER ADOPTING STIPULATION

DOCKET NO. GR05040371

(SERVICE LIST ATTACHED)

BY THE BOARD:

On April 26, 2005, Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas Company ("ETG" or "Company") filed a petition seeking authority, pursuant to N.J.A.C. 14:1-5.11, to create a Pipeline Replacement Program ("PRP") Tariff Rider. ETG proposed to create an annually adjusted tariff rider to recover the costs associated with its replacement of all of its installed 8" - 12" cast iron main throughout its service territory. Under ETG's proposal, ETG would replace approximately 88 miles of elevated pressure 8" – 12" cast iron main by the end of 2008. Once the replacement program was completed, the Company would have no 8" – 12" elevated pressure cast iron main remaining in its service territory. The Company stated that it believed that its accelerated replacement program would enhance the safety and reliability of the Company's distribution system.

The Company estimated that its accelerated replacement program would require incremental capital expenditures of approximately $42 million. Under the Company's proposed PRP tariff rider, the Company would have been permitted to make annual filings, commencing in 2006, to recover capital costs equal to its overall pre-tax rate of return and increased depreciation expense associated with the replacement facilities placed in service each year and related carrying costs.

BACKGROUND

On July 26, 2005, the Board transmitted ETG's filing to the Office of Administrative Law ("OAL") for hearing as a contested case. The matter was assigned to Administrative Law Judge ("ALJ") Diana C. Sukovich. The Company filed testimony in support of its proposal on December 15, 2005. The Division of the Ratepayer Advocate filed testimony in opposition to the Company's proposal on February 28, 2006. The Company filed rebuttal testimony on March 17, 2006. On June 30, 2006 the Board requested the return of this matter in order to assist in the expeditious resolution of this matter. After notice to the public, public hearings concerning the Company's filing were held on July 26, 2006, in Flemington, New Jersey and July 28, 2006, in Rahway, New Jersey.

STIPULATION

The parties in this proceeding, ETG, Rate Counsel[1] and the Board Staff (collectively "the Parties") reviewed financial information provided by ETG and engaged in discovery and settlement discussions. As a result of those discussions, the Parties entered into the attached stipulation ("Stipulation") that proposes to resolve the issues in this proceeding. The salient provisions of the Stipulation are summarized below:

1 PRP Tariff Rider: ETG shall not implement a PRP tariff Rider.

2. Accelerated Replacement of 8" Elevated Pressure Cast Iron Main: The Company has approximately 60 miles of elevated pressure 8" cast iron main presently installed in its service territory. The Company shall use its commercially reasonable best efforts to replace all of its elevated pressure 8" cast iron main presently installed in its service territory, as well as any unanticipated 10" – 12" cast iron main that is integral to the replacement of the 8" main by June 30, 2010 with 10% of the 8" main replaced in 2006, 10% replaced in 2007, 30% replaced in 2008, 40% replaced in 2009, and the remaining 10% replaced by June 30, 2010. The Company may accelerate this schedule for operational purposes, but not for deferral/cost recovery purposes.

3. Deferral Authority: As of the effective date of this Board Order ("Effective Date"), the Company shall have the authority to defer for future recovery in base rates the following revenue requirement-related costs associated with replacement mains and certain replacement services that will be placed in service to replace the existing elevated pressure 8" cast iron main as well as any unanticipated 10"-12" elevated pressure cast iron main that is integral to the replacement of the 8" main (hereinafter the costs of these replacement facilities shall be referred to as "Eligible Investments"):

   (a) carrying costs shall be equal to the return on seven-year United States Treasury securities plus sixty basis points, as determined from the Federal Reserve Statistical Release published on or closest to August 31 of each year ("SBC Rate"); and

   (b) depreciation expense will be calculated at the current rates approved by the Board

   Carrying costs shall be applied to the net plant-in-service balance (plant offset by accumulated depreciation and accumulated deferred income taxes) on a monthly basis. Eligible Investments shall not include the costs of meters, replacing meters, the costs of removing old pipe or the costs of replacing services that normally would not be replaced as part of a main replacement project.

   In addition, during each of calendar year 2007 and 2008, deferral of the costs of replacing 8" elevated pressure cast iron main shall not commence until ETG's Eligible Investments for such costs exceed $674,251 in 2007 and $2,431,417 in 2008, respectively. The carrying costs and depreciation expenses associated with (i) the first $674,251 of Eligible Investments in 2007 and (ii) the first $2,431,417 of Eligible Investments in 2008 shall not be eligible for deferral. The carrying costs and depreciation expense associated with Eligible Investments in excess of these threshold amounts in each year shall be eligible for deferral. In 2006, there is no threshold amount. The 2007 and 2008 thresholds are designed so that once the replacement of the 4" - 6" pipeline should be completed, deferral of the costs associated with ETG's 8" pipeline replacement shall be permitted only to the extent that

[1] The Division of the Ratepayer Advocate is now known as the "Department of the Public Advocate, Division of Rate Counsel" (hereinafter "Rate Counsel").

these costs exceed the average annual amounts that were previously spent to replace the 4-6" pipe.

No Eligible Investments incurred in 2009 or 2010 shall be eligible for deferral under this Stipulation. Instead, it is the Parties' intent that the costs and expenses associated with Eligible Investments in 2009 and 2010 shall be treated in accordance with normal ratemaking practices in the Company's 2009 rate case.

ETG's authority to defer the costs of Eligible Investments shall expire on the effective date of new base rates resulting from its 2009 rate case. ETG shall be permitted to include the costs of any Eligible Investments in future base rates in accordance with normal ratemaking practice.

In addition to replacing the 8" elevated pressure cast iron main, the Company shall use its commercially reasonable best efforts to complete the replacement of all of its existing 4" – 6" elevated pressure cast iron main by December 31, 2007 as per a prior commitment. If the Company does not complete the replacement of all of its 4" – 6" elevated pressure cast iron main by June 30, 2008, the Company shall cease prospectively deferring costs associated with Eligible Investments until such time as replacement of the 4" – 6" elevated pressure cast iron main is complete, unless Board Staff and Rate Counsel agree otherwise in writing.

Finally, to the extent that the Company projects that the balance of deferred costs associated with Eligible Investments will exceed $1.5 million, the Company shall notify Staff and Rate Counsel in writing that the $1.5 million threshold will be exceeded. The Company shall not be permitted to defer more than $1.5 million in total unless and until the Company notifies Staff and Rate Counsel in writing that this threshold is likely to be or has been exceeded.

4. Earnings Cap: ETG shall not be permitted to defer any costs associated with Eligible Investments to the extent that such deferrals cause the Company to earn an annual calendar year return on equity in excess of the ten percent (10%) return on equity approved by the Board in ETG's previous base rate proceeding in Docket No. GR02004024. In calculating earnings, costs and expenses (i.e. debt costs and depreciation expense associated with Eligible Investments) shall be included in the earnings calculation.

5. Reporting Requirements: ETG shall file semiannual PRP reports no later than March 1 and September 1 of each year with the Board Staff and Rate Counsel.

6. PRP-Related Issues to be Addressed In The Company's 2009 Rate Case: In ETG's 2009 base rate case, ETG shall be permitted to recover all prudent and reasonable costs deferred in accordance with the terms of this Stipulation. However, issues to be addressed in connection with the recovery of the costs deferred in accordance with this Stipulation include, but are not limited to:

   (a) the determination of an appropriate period for recovering the deferred costs;

   (b) the appropriate amortization of the deferred costs;

   (c) whether the deferred costs were properly calculated in accordance with this Stipulation: and

   (d) the customer classes from which deferred costs should be recovered.

7. Withdrawal From The Transmission Portion Of The Joint Pipeline Integrity Management Proceeding: On October 14, 2005, ETG and the State's other gas distribution companies filed a petition in Docket No. GO05100879 seeking to defer and recover outside of a base rate case certain transmission costs associated with compliance with the Department of Transportation's Pipeline Integrity Management Program ("PIM"). ETG shall withdraw from the proceeding insofar as it addresses recovery of transmission-related PIM costs. However, ETG may participate as a petitioner in any effort to seek deferral and recovery of costs that may be incurred to recover distribution-related costs that may be incurred in the future to comply with any federal programs, similar to the PIM, that may apply to distribution facilities.

DISCUSSION AND FINDINGS

The Board's Bureau of Pipeline Safety Staff has been monitoring the aging cast iron pipelines of ETG, particularly the high pressure, smaller diameter mains that have exhibited the greatest failure rates leading to both potential and actual hazards. Because of Staff's safety concerns, ETG previously agreed to accelerate the replacement of all 4" through 6" high pressure cast iron mains so that all mains within this group would be replaced by the year 2008. Once completed, the company planned to systematically replace all of the high pressure 8" cast iron pipelines, which presented the next most frequent failure rates due to breaks.

This course of action is consistent with the recommendations and findings presented in the December 2005 "Integrity Management for Gas Distribution Pipelines Report of Phase 1 Investigations" which was developed in response to a request from Congress. Specifically, as stated in Exhibit E, Subpart O, priority replacement of "....[c]ast iron, focusing first on small diameter (8" and less), higher pressures...." is the consensus of state regulatory officials.

However, in light of several recent incidents involving breaks on 8" high pressure cast iron main, including the natural gas explosion of January 31, 2005 on Lehigh Avenue in Union, New Jersey, it has become apparent that the replacement of ETG's 60 miles of elevated pressure 8" cast iron main presently should begin prior to the previously planned replacement schedule. Therefore, the Board **FINDS** that approval of the Stipulation, which provides that the Company will replace all of its 8" cast iron main by June 30, 2010, will enhance the safety and reliability of ETG's distribution system.

Utilities in this state are responsible for providing safe and reliable service. The replacement of ETG's 8" pipeline pursuant to the Stipulation will enhance the safety and reliability of ETG's distribution system. Normally, pipeline replacement costs such as these should be recovered through base rate proceedings as should other costs associated with providing safe and reliable service. However, there are unique circumstances that warrant special treatment in this proceeding. First is the fact that pursuant to the Board's November 17, 2004 Order in Docket No. GM04070721, ETG is restricted from filing a base rate case that would increase rates prior to January 2010. This, coupled with the fact that ETG renewed its commitment to its 4"-6" pipeline replacement program, for which it does not receive special rate treatment, influenced the Board's consideration of special treatment for this second pipeline replacement program. Further, once the replacement of the 4"-6" pipeline should be completed, the Stipulation provides for deferral of the costs associated with ETG's 8" pipeline replacement only to the extent that these costs exceed the average annual amounts that were previously spent to replace the 4-6" pipe. Additionally, the Stipulation provides that costs associated with replacements after December 31, 2008 will not be deferred as ETG's base rate stay out will end shortly thereafter and these costs can be addressed on a timely basis through normal ratemaking practices. Therefore, the Board **FINDS** that there are unique circumstances in this proceeding which make it reasonable to consider deferred accounting treatment for these costs.

The Board has reviewed the details of the deferral mechanism provided for by the Stipulation. These details include, but are not limited to a) the deferral of carrying costs on the net plant-in-service balance equal to the annual return on seven-year United States Treasury securities plus sixty basis points; b) the deferral of depreciation expenses that are calculated at the current rates approved by the Board; c) no deferral for the costs of replacing meters, the costs of removing old pipe, the costs of replacing services that normally would not be replaced as part of a main replacement project, or costs associated with the replacement of pipe after December 31, 2008; and d) an earnings cap that is set at ETG's authorized return on equity from its last base rate case. Based upon the Board's review of the deferral mechanism as a whole, the Board **FINDS** that the deferral mechanism provided for by the Stipulation is reasonable.

Therefore, the Board **HEREBY ADOPTS** the attached Stipulation and incorporates by reference its terms and conditions as if fully set forth herein.

The Board emphasizes that while the Stipulation provides for specific timeframes for the replacement of certain categories of ETG's pipeline, ETG's is entirely responsible for ensuring the safety and reliability of its entire pipeline system. The Board's adoption of the Stipulation does not in any way reduce this obligation nor does it eliminate ETG's responsibility to replace its 4"-6" pipeline or its 8" pipeline sooner than may be required by the Stipulation or its responsibility to replace other categories of its pipeline if needed to ensure that its distribution system is safe and reliable.

DATED: 8/18/06

BOARD OF PUBLIC UTILITIES
BY:

Jeanne M. Fox

JEANNE M. FOX
PRESIDENT

Frederick F. Butler

FREDERICK F. BUTLER
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COMMISSIONER

ATTEST:

Kristi Izzo

KRISTI IZZO
SECRETARY

I HEREBY CERTIFY that the within document is a true copy of the original in the files of the Board of Public Utilities

Kristi Izzo

2D

Elizabethtown Gas

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August 15, 2006

Via Federal Express

Honorable Kristi Izzo
Secretary
State of New Jersey
Board of Public Utilities
Two Gateway Center
Newark, New Jersey 07102

Re: In the Matter of the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas Company Request to Establish A Pipeline Replacement Program Cost Recovery Rider BPU Docket No. GR05040371

Dear Secretary Izzo

Enclosed for filing in the above proceeding are an original and ten copies of a Stipulation executed by Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas ("Elizabethtown"), the Staff of the Board of Public Utilities and the Department of the Public Advocate, Division of Rate Counsel, the only current parties to the above proceeding. Elizabethtown requests the Board of Public Utilities to consider and approve the Stipulation at its earliest convenience.

If you have any questions concerning the Stipulation, please contact the undersigned. Thank you for your attention in this matter.

Yours truly,

Mary Patricia Keefe

Mary Patricia Keefe,
Director, Regulatory Affairs

cc: Service List

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STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

In the Matter of the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas Company To Establish A Pipeline Replacement Program Cost Recovery Rider	))))	**BPU Docket No. GR05040371** **STIPULATION**

Background

On April 26, 2005, Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas ("Elizabethtown" or "Company") filed a petition in the above proceeding seeking authority pursuant to *N.J.A.C.* 14:1-5.11 to implement a Pipeline Replacement Program ("PRP") Tariff Rider. Under the proposed Tariff Rider, Elizabethtown would be permitted to make annual filings to recover capital costs, increased depreciation expense and certain related carrying costs associated with a program to replace over a three-year period approximately eighty-eight (88) miles of elevated pressure 8-12-inch cast iron main. Once the replacement program was completed, the Company would have no 8-12-inch elevated pressure cast iron main remaining in its service territory.

The Company stated that its elevated pressure cast iron distribution main was installed many years ago. As this type of pipe ages, under certain conditions, it becomes more prone to graphitic corrosion, a condition which can render the pipe more vulnerable to leaks and cracks. While the Company periodically replaces portions of its 8-12-inch elevated pressure main in compliance with applicable safety regulations and/or the Company's operating standards, the Company has had no systematic replacement program for replacing 8-12-inch elevated pressure cast iron main. In contrast, the Company has had a program of systematically replacing 4-6-inch elevated pressure cast iron main. Under this plan, the Company will essentially complete the replacement of all 4-6-inch elevated pressure cast iron main by the end of 2007

Under the Company's proposal, the Company would have committed to using its commercially reasonable best efforts to replace its 8-12-inch elevated pressure cast iron main by the end of 2008. The

Company stated that it believed that its accelerated replacement program would enhance the safety and reliability of the Company's distribution system. The Company estimated that its accelerated replacement program would require incremental capital expenditures of approximately $42 million.

Under the Company's proposed PRP tariff rider, the Company would have been permitted to make annual filings commencing in 2006 to recover capital costs equal to its overall pre-tax rate of return and increased depreciation expense associated with the replacement facilities placed in service each year and related carrying costs. Under the Company's proposal, the replacement facilities would include the costs of replacement mains and appurtenant facilities such as services and meters. The Company would have been permitted to make annual PRP filings until new base rates became effective in its next base rate case, which is required to be filed in March, 2009 for rates to be effective in January, 2010. The PRP would terminate at the time new base rates became effective and any unrecovered PRP amounts would be rolled into base rates in the 2009-2010 base rate proceeding.

The Company's petition was transmitted to the Office of Administrative Law as a contested case on July 26, 2005. The Company filed testimony in support of its proposal on December 15, 2005. Division of the Ratepayer Advocate[1] filed testimony in opposition to the Company's proposal on February 28, 2006. The Company filed rebuttal testimony on March 17, 2006. After notice to the public, public hearings concerning the Company's filing were held on July 26, 2006 in Flemington, New Jersey and July 28, 2006 in Rahway, New Jersey. The Board's Staff and Rate Counsel, with the Company, the only parties to this proceeding (collectively, the Parties), have conducted extensive discovery and held settlement conferences to discuss the matters at issue in this proceeding. On June 26, 2006, the Office of Pipeline Safety submitted a letter to the Parties in which the Office recommended an accelerated program of replacement of cast iron pipe. This letter is attached hereto as Attachment A. As a result of those discussions and the letter from the Office of Pipeline Safety, the Parties have resolved all remaining issues in this proceeding in accordance with the Stipulation set forth below.

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[1] The Division of the Ratepayer Advocate is now known as the "Department of the Public Advocate, Division of Rate Counsel" (hereinafter "Rate Counsel").

Stipulation

Based upon and subject to the terms and conditions set forth herein, the Board Staff, Rate Counsel and Elizabethtown stipulate as follows:

1. **PRP Tariff Rider:** Elizabethtown shall not implement a PRP tariff Rider.

2. **Accelerated Replacement Of 8-inch Elevated Pressure Cast Iron Main.** The Company has approximately sixty (60) miles of elevated pressure 8-inch cast iron main presently installed in its service territory. The Company shall use its commercially reasonable best efforts to replace all of its elevated pressure 8-inch cast iron main presently installed in its service territory, as well as any unanticipated, incidental 10-12-inch cast iron main encountered during the 8-inch replacement program, by June 30, 2010 in accordance with the following calendar year schedule:

(a) 2006 – 10% of 8-inch elevated pressure mains replaced as prioritized by the Company;

(b) 2007 – 10% of 8-inch elevated pressure mains replaced as prioritized by the Company;

(c) 2008 – 30% of 8-inch elevated pressure mains replaced as prioritized by the Company;

(d) 2009 – 40% of 8-inch elevated pressure mains replaced as prioritized by the Company; and

(e) January 1, 2010 – June 30, 2010 – remaining 10% of 8-inch elevated pressure mains replaced.

The Company is permitted to accelerate this schedule for operational purposes, but not for deferral/cost recovery purposes as set forth below.

3. **Deferral Authority.** As of the effective date of a Board Order approving this stipulation ("Effective Date"), the Company shall have the authority to defer for future recovery in base rates the following revenue requirement-related costs associated with replacement mains and certain replacement services that will be placed in service to replace the existing elevated pressure 8–inch cast iron main as

well as any unanticipated,10-12-inch elevated pressure cast iron main that is integral to the replacement of the 8-inch mains. (hereinafter the costs of these replacement facilities shall be referred to as "Eligible Investments"):

(a) carrying costs equal to the return on seven-year United States Treasury securities plus sixty basis points, as determined from the Federal Reserve Statistical Release published on or closest to August 31 of each year ("SBC Rate"); and

(b) depreciation expense calculated at the current rates approved by the Board.

For the purpose of calculating the deferred amounts, carrying costs and depreciation expense shall be calculated from the first day of the month following the month in which replacement facilities are placed in service. Annual carrying costs shall be determined based on the monthly defined amounts in accordance with the following formula:

[[Eligible Investments – Accumulated Depreciation – Accumulated Deferred Income Taxes] x After Tax Rate of Return x Revenue Adjustment Factor + [Eligible Investments x Depreciation Rate]]/12: where

(i) the After Tax Rate of Return = (SBC Rate x (1 – Income Tax Rate) (currently 4.53% x 1-.4085)= 2.68%; and

(ii) the current Revenue Factor = 1.71700

For the purpose of applying the above-formula, Eligible Investments shall include the costs of replacement mains and the costs of replacement services that are normally replaced by the Company when it replaces mains, such as bare steel services. Eligible Investments shall not include the costs of meters, replacing meters, the costs of removing old pipe or the costs of replacing services that normally would not be replaced as part of a main replacement project.

In addition, during each of calendar year 2007 and 2008, deferral of the costs of replacing eight-inch elevated pressure cast iron main shall not commence until Elizabethtown's Eligible Investments for such costs exceed $674,251 in 2007 and $2,431,417 in 2008, respectively. The carrying costs and depreciation expenses associated with (i) the first $674,251 of Eligible Investments in 2007 and (ii) the first $2,431,417 of Eligible Investments in 2008 shall not be eligible for deferral. The carrying costs and depreciation expense associated with Eligible Investments in excess of these threshold amounts in each year shall be eligible for deferral. In 2006, there is no threshold amount.

No Eligible Investments incurred in 2009 or 2010 shall be eligible for deferral under this Stipulation. Instead, it is the Parties' intent that the costs and expenses associated with Eligible Investments in 2009 and 2010 shall be treated in accordance with normal ratemaking practices in the Company's 2009 rate case.

Elizabethtown's authority to defer the costs of Eligible Investments shall expire on the effective date of new base rates resulting from its 2009 rate case. Elizabethtown shall be permitted to include the costs of any Eligible Investments in future base rates in accordance with normal ratemaking practice.

In addition to replacing the 8-inch elevated pressure cast iron main, the Company shall use its commercially reasonable best efforts to complete the replacement of all existing 4-6-inch elevated pressure cast iron main by December 31, 2007. However, it is anticipated that there may be short segments of this main remaining (typically fifty (50) feet in length or less), that are connected to 8-inch elevated pressure cast iron main. These short segments of 4–6-inch elevated pressure main shall be replaced by no later than June 30, 2008, in conjunction with the 8-inch elevated pressure cast iron main segments that they are connected to. If Elizabethtown does not complete the replacement of all of its 4-6-inch main by December 31, 2007, they shall provide a report to the parties by January 15, 2008 identifying which sections they could not feasibly replace by December 31, 2007 and provide the justification as to why it was not feasible to complete such sections. If the Company does not complete the replacement of all of its 4-6-inch elevated pressure cast iron main by June 30, 2008, the Company shall cease prospectively deferring costs associated with Eligible Investments until such time as replacement of the 4-6-inch elevated pressure cast iron main is complete, unless Board Staff and Rate Counsel agree otherwise in writing.

Finally, to the extent that the Company projects that the balance of deferred costs associated with Eligible Investments will exceed $1.5 million, the Company shall notify Staff and Rate Counsel in writing that the $1.5 million threshold will be exceeded. The Company shall not be permitted to defer more than $1.5 million unless and until the Company notifies Staff and Rate Counsel in writing that this threshold is likely to be or has been exceeded.

4. **Earnings Cap.** Elizabethtown shall not be permitted to defer any costs associated with Eligible Investments to the extent that such deferrals cause the Company to earn an annual calendar year return on equity in excess of the ten percent (10%) return on equity approved by the Board in Elizabethtown's previous base rate proceeding in Docket No. GR02004024. In calculating earnings, costs and expenses (*i.e.* debt costs and depreciation expense associated with Eligible Investments) shall be included in the earnings calculation.

5. **Reporting Requirements.** Elizabethtown shall file semiannual PRP reports with the Board and Rate Counsel no later than March 1 and September of each year setting forth for the prior periods ending December 31 and June 30, respectively (i) the amount and cost of replacement activities completed during the six (6) month reporting period, (ii) the total cumulative amount and cost of replacements completed through the end of the reporting period, (iii) the amount and projected cost of the facilities to be completed over the next six (6) month period, (iv) any revisions to the projected costs and timing of completing the remainder of the replacement project, (v) the amount deferred through the end of the reporting period, and (vi) an estimate of the total deferred amount associated with Eligible Investments that the Company will have on its books at December 31, 2009. Attached to this Stipulation as Appendix C is an estimate of the amounts that will be deferred pursuant to this Stipulation. The Company shall provide an update of this schedule with each of its semi-annual PRP reports. The updated schedule shall include actual numbers for the time period covered by the semi-annual PRP report and updated estimates for the remaining period. Estimated and actual numbers shall be identified as such in the report. The semi-annual PRP reports shall include documentation in support of the depreciation rates used as well as a copy of the Federal Reserve Statistical Report that the present SBC rate is based upon. The semi-annual PRP reports shall include a narrative describing the location of the pipe that was

replaced during the six month period and why it was prioritized for replacement. Elizabethtown's March reports shall also include earnings sharing calculations in the Form attached as Appendix B

6. **<u>PRP-Related Issues To Be Addressed In The Company's 2009 Rate Case</u>.** In Elizabethtown's 2009 base rate case, Elizabethtown shall be permitted to recover all prudent and reasonable costs deferred in accordance with the terms of this Stipulation. However, issues to be addressed in connection with the recovery of the costs deferred in accordance with this Stipulation include, but are not limited to:

(a) the determination of an appropriate period for recovering the deferred costs;

(b) the appropriate amortization of the deferred costs;

(c) whether the deferred costs were properly calculated in accordance with this Stipulation; and

(d) the customer classes from which deferred costs should be recovered.

7. **<u>Withdrawal From The Transmission Portion Of The Joint Pipeline Integrity Management Proceeding</u>.** On October 14, 2005, Elizabethtown and the State's other gas distribution companies filed a petition in Docket No. GO05100879 seeking to defer and recover outside of a base rate case certain transmission costs associated with compliance with the Department of Transportation's Pipeline Integrity Management Program ("PIM") Elizabethtown shall withdraw from the proceeding insofar as it addresses recovery of transmission-related PIM costs. However, Elizabethtown may participate as a petitioner in any effort to seek deferral and recovery of costs that may be incurred to recover distribution-related costs that may be incurred in the future to comply with any federal programs, similar to the PIM, that may apply to distribution facilities.

8. **<u>Unique Circumstances</u>.** This Stipulation is the product of unique circumstances, and, as such, shall not be used as precedent in any other proceeding to justify any requested relief. The unique circumstances that have caused the parties to agree to this Stipulation include the facts that:

(a) Elizabethtown is subject to a base rate stay out through 2009;

(b) Elizabethtown has an obligation to file a base rate case in 2009;

(c) Elizabethtown is subject to earnings sharing in 2008 and 2009;

(d)

(d) Elizabethtown presently has an accelerated replacement program for its 4-6-inch elevated pressure cast iron pipe for which it is not receiving special rate treatment. The deferral mechanism provided for in this stipulation only addresses costs above those incurred for normal ongoing replacements and above Elizabethtown's average annual spending associated with its accelerated replacement program for its 4-6-inch elevated pressure cast iron pipe; and

(e) The deferral mechanism provided for in this stipulation does not provide for deferral of costs associated with replacements after December 31, 2008 as Elizabethtown's base rate stay out will end and these costs can be addressed in a timely basis through normal ratemaking practices.

Notwithstanding this Stipulation, pipeline replacement costs should normally be recovered through base rate proceedings.

9. **Entirety Of Stipulation.** This Stipulation represents a mutual balancing of interests and, therefore, is intended to be accepted and approved in its entirety. In the event that the Board does not adopt this Stipulation in its entirety in an Order, then any Party hereto is free to pursue its then available legal remedies with respect to all issues in this Stipulation as though this Stipulation had not been signed.

10. **Binding Effect.** It is the intent of the Parties that the provisions hereof be approved by the Board, as appropriate, as being in the public interest. The Parties further agree that they consider the Stipulation to be binding on them for all purposes herein.

11. **General Reservation.** It is specifically understood and agreed that this Stipulation represents a negotiated agreement and has been made exclusively for the purpose of this proceeding. Except as expressly provided herein, neither Elizabethtown, the Board, its Staff, the Rate Counsel nor any

other party shall be deemed to have approved, agreed to, or consented to any principle or methodology underlying or supposed to underlie any agreement provided herein.

WHEREFORE, the Parties hereto do respectfully submit this Stipulation to the Board of Public Utilities and request the Board to issue a Decision and Order approving this Stipulation in accordance with the terms thereof.

PIVOTAL UTILITY HOLDINGS, INC.
D/B/A ELIZABETHTOWN GAS

By: Mary Patricia Keefe
Mary Patricia Keefe
Director – Regulatory Affairs

~~**DEPARTMENT OF THE PUBLIC ADVOCATE**~~
~~**DIVISION OF RATE COUNSEL**~~

~~By: __________~~
~~Seema Singh~~
~~Director~~

STAFF OF THE BOARD OF PUBLIC UTILITIES

BT By: Babette Tenzer C. DAG
Ry: Zulima Farber
Attorney General of New Jersey

By: Babette Tenzer

DEPARTMENT OF PUBLIC ADVOCATE
DIVISION OF RATE COUNSEL

By: Felicia Thomas-Friel
Felicia Thomas-Friel, Esq.
Div. of Rate Counsel

Dated: __________
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State of New Jersey
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102

Nusha Wyner, Director
Division of Energy

Tel. # (973) 648-[illegible]
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June 26, 2006

Felicia Thomas-Friel, Esq.
Division of the Ratepayer Advocate
31 Clinton Street, 11th Floor
P.O. Box 45029
Newark, NJ07101

Judith Appel, Esq.
Division of the Ratepayer Advocate
31 Clinton Street, 11th Floor
P.O. Box 46005
Newark, NJ 07101

Re: I/M/O the Petition of Pivotal Utility Holdings, Inc. d/b/a Elizabethtown Gas Company to Establish a Pipeline Replacement Program Cost Recovery Rider. BPU Docket No. GR05040371

Dear Felicia and Judy:

The Bureau of Pipeline Safety (BPS) has been monitoring the aging cast iron pipelines of Elizabethtown Gas Company, particularly the high pressure, smaller diameter mains that have exhibited the greatest failure rates, leading to both potential and actual hazards. Because of our safety concerns, the Company agreed to accelerate the replacement of all 4" through 6" high pressure cast iron so that all mains within this group would be replaced by the year 2008. Once completed, the company planned to systematically replace all of the high pressure 8" cast iron pipelines, which presented the next most frequent failure rates due to breaks.

This course of action is consistent with the recommendations and findings presented in the December 2005 "Integrity Management for Gas Distribution Pipelines Report of Phase 1 Investigations" which was developed in response to a request from Congress. Specifically, as stated in Exhibit E, Subpart O, priority replacement of "....[c]ast iron, focusing first on small diameter (8" and less), higher pressures...." is the consensus of state regulatory officials.

In light of several recent incidents involving breaks on 8" high pressure cast iron main, including the natural gas explosion of January 31, 2005 on Lehigh Avenue in Union, New Jersey, it has become apparent to the Bureau of Pipeline Safety that the replacement of this group of pipe should begin prior to the planned replacement schedule. Staff recommends that an accelerated program to replace all of the 8" high pressure cast iron be implemented at this time, which will enhance the safety and reliability of the Elizabethtown distribution system.

The BPS will continue to monitor the replacement of the 8" cast iron and will closely monitor the failure and breakage of this group of pipe and take further appropriate action should conditions warrant.

Sincerely,

Edward Lihan

Edward Lihan, Acting Bureau Chief
Pipeline Safety

c: Service List

Pivotal Utility Holdings, Inc.
d/b/a Elizabethtown Gas

Earnings Report
Twelve Months Ended November 30, 2005

1.	**Regulated Jurisdictional Net Income[A]**			**$14,119,615**
2.	**Average Thirteen Month Equity Balance[B]**			**$220,956,212**
3.	**Return On Equity[C]**			
4.	**Jurisdictional Return On Rate Base[D]**			
5.	**Current Public Credit Ratings**	**A.**	**Standard & Poor's**	**A-**
		B.	**Moody's**	**A3**

The above ratings are for Pivotal Utility Holdings Inc.

A. The Company's Regulated Jurisdictional Net Income is calculated by subtracting from total net income (i) margins retained by the Company from non-firm sales and transportation services and off-system sales and capacity release, net of associated taxes, and (ii) net income derived from unregulated activities conducted by Elizabethtown. The calculation of Regulated Jurisdictional Net Income excludes any expenses associated with the amortization of "Goodwill."

B. The Company's average thirteen month common equity balance for any annual period is the Company's average total common equity less the Company's average common equity investment in unregulated subsidiaries, if any.

C. The Company's rate of return on common equity is calculated by dividing the Company's Regulated Jurisdictional Net Income by the Company's average thirteen month total common equity balance.

D. Jurisdictional Return on Rate Base is calculated by dividing the Company's Regulated Jurisdictional Net Income by Company's calculation of Rate Base. The calculation of Rate Base is equal to the sum of:
   (i) The 13 – month average balance of net plant;
   (ii) The thirteen month average balance of (a) Materials and Supplies, (b) Fuel Inventory, (c) Prepaid Pension, (d) Customer Advance For Construction, (e) Deferred Credits, (f) Deferred Income Taxes; and (g) deferred credits related to the Comfort Care program.
   (iii) A working capital allowance of $22,056,000 which is the working capital allowance reflected in Elizabethtown's previous base rate filing in BPU Docket No. GR02040245.

ETG PRP Deferral

Projected Cost - 8" Mains	15,829,440		
Projected Cost - 8" Servic	4,088,400	Book Depreciation Rate =	2.14%
Total	19,917,840	Tax Depreciation Rate =	6.67%

*Formula = (EI-ADEP-ADIT)*ATROR*RAF+EI*DEP*

Annual 4& 6 Threshold, Weighted Avg. Cost of Debt, & After Tax Rate of Return:				
2007	674,251	4.53%	2.68%	(4.53%*(1-0.4085))
2008	2,431,417	5.63%	3.33%	(5.63%*(1-0.4085))

M/E	Y	M		%	Monthly Main/Service Cost	Monthly Non-eligible Up to 4&6	Eligible Investment To Date	Accum. Deprec.	Accum. Deferred Income Tax	After Tax Rate of Return	Revenue Factor	Eligible Investment	Deprec. Rate	Monthly Deferral	Deferral To Date	Annual Deferral
07/31/06	1	1	1	10%	331,964		331,964	592	512	2.68%	1.71700	331,964	2.14%	1,860	1,860	
08/31/06	1	2	2	10%	331,964		663,928	1,776	1,535	2.68%	1.71700	663,928	2.14%	3,717	5,577	
09/30/06	1	3	3	10%	331,964		995,892	3,552	3,069	3.33%	1.71700	995,892	2.14%	6,490	12,067	
10/31/06	1	4	4	10%	331,964		1,327,856	5,920	5,115	3.33%	1.71700	1,327,856	2.14%	8,643	20,710	
11/30/06	1	5	5	10%	331,964		1,659,820	8,880	7,673	3.33%	1.71700	1,659,820	2.14%	10,790	31,500	
12/31/06	1	6	6	10%	331,964		1,991,784	12,432	10,742	3.33%	1.71700	1,991,784	2.14%	12,932	44,432	44,432
01/31/07	1	7	7	10%	165,982	165,982	1,991,784	15,984	13,812	3.33%	1.71700	1,991,784	2.14%	12,901	57,332	
02/28/07	1	8	8	10%	165,982	165,982	1,991,784	19,536	16,881	3.33%	1.71700	1,991,784	2.14%	12,869	70,201	
03/31/07	1	9	9	10%	165,982	165,982	1,991,784	23,088	19,950	3.33%	1.71700	1,991,784	2.14%	12,838	83,039	
04/30/07	1	10	10	10%	165,982	165,982	1,991,784	26,640	23,019	3.33%	1.71700	1,991,784	2.14%	12,806	95,845	
05/31/07	1	11	11	10%	165,982	10,323	2,147,443	30,470	26,328	3.33%	1.71700	2,147,443	2.14%	13,791	109,636	
06/30/07	1	12	12	10%	165,982	-	2,313,425	34,595	29,893	3.33%	1.71700	2,313,425	2.14%	14,842	124,478	
07/31/07	2	1	13	10%	165,982	-	2,479,407	39,017	33,714	3.33%	1.71700	2,479,407	2.14%	15,889	140,367	
08/31/07	2	2	14	10%	165,982	-	2,645,389	43,735	37,790	3.33%	1.71700	2,645,389	2.14%	16,934	157,301	
09/30/07	2	3	15	10%	165,982	-	2,811,371	48,748	42,123	3.33%	1.71700	2,811,371	2.14%	17,976	175,278	
10/31/07	2	4	16	10%	165,982	-	2,977,353	54,058	46,711	3.33%	1.71700	2,077,353	2.14%	19,016	194,294	
11/30/07	2	5	17	10%	165,982	-	3,143,335	59,663	51,554	3.33%	1.71700	3,143,335	2.14%	20,053	214,347	
12/31/07	2	6	18	10%	165,982	-	3,309,317	65,565	56,654	3.33%	1.71700	3,309,317	2.14%	21,088	235,435	191,003
01/31/08	2	7	19	30%	497,946	497,946	3,309,317	71,467	61,753	3.33%	1.71700	3,309,317	2.14%	21,035	256,470	
02/29/08	2	8	20	30%	497,946	497,946	3,309,317	77,368	66,853	3.33%	1.71700	3,309,317	2.14%	20,983	277,453	
03/31/08	2	9	21	30%	497,946	497,946	3,309,317	83,270	71,952	3.33%	1.71700	3,309,317	2.14%	20,931	298,384	
04/30/08	2	10	22	30%	497,946	497,946	3,309,317	89,171	77,052	3.33%	1.71700	3,309,317	2.14%	20,878	319,262	
05/31/08	2	11	23	30%	497,946	439,633	3,367,630	95,177	82,241	3.33%	1.71700	3,367,630	2.14%	21,207	340,468	
06/30/08	2	12	24	30%	497,946	-	3,865,576	102,071	88,198	3.33%	1.71700	3,865,576	2.14%	24,406	364,874	
07/31/08	3	1	25	30%	497,946	-	4,363,522	109,852	94,922	3.33%	1.71700	4,363,522	2.14%	27,598	392,472	
08/31/08	3	2	26	30%	497,946	-	4,861,468	118,522	102,413	3.33%	1.71700	4,861,468	2.14%	30,781	423,253	
09/30/08	3	3	27	30%	497,946	-	5,359,414	128,080	110,672	3.33%	1.71700	5,359,414	2.14%	33,957	457,210	
10/31/08	3	4	28	30%	497,946	-	5,857,360	138,525	119,698	3.33%	1.71700	5,857,360	2.14%	37,125	494,335	
11/30/08	3	5	29	30%	497,946	-	6,355,306	149,859	129,491	3.33%	1.71700	6,355,306	2.14%	40,285	534,620	
12/31/08	3	6	30	30%	497,946	-	6,853,252	162,080	140,051	3.33%	1.71700	6,853,252	2.14%	43,437	578,057	342,622
01/31/09	3	7	31				6,853,252	174,302	150,612	3.33%	1.71700	6,853,252	2.14%	43,328	621,385	
02/28/09	3	8	32				6,853,252	186,524	161,172	3.33%	1.71700	6,853,252	2.14%	43,220	664,605	
03/31/09	3	9	33				6,853,252	198,745	171,733	3.33%	1.71700	6,853,252	2.14%	43,111	707,716	
04/30/09	3	10	34				6,853,252	210,967	182,294	3.33%	1.71700	6,853,252	2.14%	43,003	750,719	
05/31/09	3	11	35				6,853,252	223,189	192,854	3.33%	1.71700	6,853,252	2.14%	42,894	793,613	
06/30/09	3	12	36				6,853,252	235,410	203,415	3.33%	1.71700	6,853,252	2.14%	42,786	836,399	
07/31/09	4	1	37				6,853,252	247,632	213,975	3.33%	1.71700	6,853,252	2.14%	42,677	879,076	
08/31/09	4	2	38				6,853,252	259,853	224,536	3.33%	1.71700	6,853,252	2.14%	42,569	921,644	
09/30/09	4	3	39				6,853,252	272,075	235,096	3.33%	1.71700	6,853,252	2.14%	42,460	964,104	
10/31/09	4	4	40				6,853,252	284,297	245,657	3.33%	1.71700	6,853,252	2.14%	42,351	1,006,456	
11/30/09	4	5	41				6,853,252	296,518	256,217	3.33%	1.71700	6,853,252	2.14%	42,243	1,048,699	
12/31/09	4	6	42				6,853,252	308,740	266,778	3.33%	1.71700	6,853,252	2.14%	42,134	1,090,833	512,776

ost -8" Mains
ost - 8" Services

Depreciation and Deferred Tax Back-up

Y	M		Eligible Investment	This Month's Book Depreciation@ 2.14%	This Month's Tax Depreciation @ 6.67%	Difference	Deferred Income Taxes @ 40.85%	Accumulated Deferred Income Taxes	Accumulated Book Depreciation
				592	1,844	1,252	512	512	592
	2	2							
1	3	3	995,892	1,776	5,533	3,757	1,535	3,069	3,552
1	4	4	1,327,856	2,368	7,377	5,009	2,046	5,115	5,920
1	5	5	1,659,820	2,960	9,221	6,261	2,558	7,673	8,880
1	6	6	1,991,784	3,552	11,065	7,513	3,069	10,742	12,432
1	7	7	1,991,784	3,552	11,065	7,513	3,069	13,812	15,984
1	8	8	1,991,784	3,552	11,065	7,513	3,069	16,881	19,536
1	9	9	1,991,784	3,552	11,065	7,513	3,069	19,950	23,088
1	10	10	1,991,784	3,552	11,065	7,513	3,069	23,019	26,640
1	11	11	2,147,443	3,830	11,930	8,101	3,309	26,328	30,470
1	12	12	2,313,425	4,126	12,852	8,727	3,565	29,893	34,595
2	1	13	2,479,407	4,422	13,774	9,353	3,821	33,714	39,017
2	2	14	2,645,389	4,718	14,697	9,979	4,076	37,790	43,735
2	3	15	2,811,371	5,014	15,619	10,605	4,332	42,123	48,748
2	4	16	2,977,353	5,310	16,541	11,231	4,588	46,711	54,058
2	5	17	3,143,335	5,606	17,463	11,857	4,844	51,554	59,663
2	6	18	3,309,317	5,902	18,385	12,483	5,100	56,654	65,565
2	7	19	3,309,317	5,902	18,385	12,483	5,100	61,753	71,467
2	8	20	3,309,317	5,902	18,385	12,483	5,100	66,853	77,368
2	9	21	3,309,317	5,902	18,385	12,483	5,100	71,952	83,270
2	10	22	3,309,317	5,902	18,385	12,483	5,100	77,052	89,171
2	11	23	3,367,630	6,006	18,709	12,703	5,189	82,241	95,177
2	12	24	3,865,576	6,894	21,475	14,582	5,957	88,198	102,071
3	1	25	4,363,522	7,782	24,242	16,460	6,724	94,922	109,852
3	2	26	4,861,468	8,670	27,008	18,339	7,491	102,413	118,522
3	3	27	5,359,414	9,558	29,775	20,217	8,259	110,672	128,080
3	4	28	5,857,360	10,446	32,541	22,095	9,026	119,698	138,525
3	5	29	6,355,306	11,334	35,307	23,974	9,793	129,491	149,859
3	6	30	6,853,252	12,222	38,074	25,852	10,561	140,051	162,080
3	7	31	6,853,252	12,222	38,074	25,852	10,561	150,612	174,302
3	8	32	6,853,252	12,222	38,074	25,852	10,561	161,172	186,524
3	9	33	6,853,252	12,222	38,074	25,852	10,561	171,733	198,745
3	10	34	6,853,252	12,222	38,074	25,852	10,561	182,294	210,967
3	11	35	6,853,252	12,222	38,074	25,852	10,561	192,854	223,189
3	12	36	6,853,252	12,222	38,074	25,852	10,561	203,415	235,410
4	1	37	6,853,252	12,222	38,074	25,852	10,561	213,975	247,632
4	2	38	6,853,252	12,222	38,074	25,852	10,561	224,536	259,853
4	3	39	6,853,252	12,222	38,074	25,852	10,561	235,096	272,075
4	4	40	6,853,252	12,222	38,074	25,852	10,561	245,657	284,297
4	5	41	6,853,252	12,222	38,074	25,852	10,561	256,217	296,518
4	6	42	6,853,252	12,222	38,074	25,852	10,561	266,778	308,740

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